

## Privatization and budget dilemma

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The fact that the draft budget may become a bone of contention is not new for Ukraine. The adoption of the country's key financial document seems to be traditionally behind the schedule, the notorious example of that being the half-year budget marathon of 1997 with the 1997 budget being approved only on June 27, 1997 by almost the minimum number of votes: 229. The 1999 budget was approved on the New Year's eve, late at night on December 31, 1998. The 2000 budget was also late: the state finally received it in mid-February 2000.

The current political process in Ukraine has been largely influenced by the "budget fever" that is in the epicenter of the parliament's and the government's lives and risks to draw the branches of power into a vicious circle of new tension. The budget dispute, based on two main claims - "the budget is unrealistic and, therefore, should not be approved in this form" and "the budget is unrealistic for it is impossible to receive the planned revenues from privatization" is becoming increasingly politicized.

### The Process

The draft budget-2001 arrived to the parliamentary committees on October 4, 2000, and consultations and bargaining between MPs and the government have continued practically non-stop since then. Although it is likely that - as head of the Parliamentary Special Commission for Privatization Oleksandr Ryabchenko believes - "this budget will still be voted for before January 1 - or even before December" (Den, October 20, 2000), the probability that the targeted budget revenue from privatization is the key issue that may delay the adoption procedure. The draft law "On the State Budget of Ukraine for 2001" plans that as much as UAH 9.2 billion (US\$ 1.5 billion) will be received from privatization. Possibly, the expected figure reflects Prime Minister Victor Yushchenko's expressed belief that the government nowadays "feels sufficient demand for the Ukrainian privatization" (Interfax-Ukraine, January 17, 2000). Currently the government takes much effort to convince the international community and, particularly, Ukrainian MPs whose support will be critical for adopting the budget, that the planned revenue is realistic. Meanwhile, Ukrainian law-makers tend to be rather skeptical about the possibility, and many of them tend to agree with parliamentary majority coordinator Oleksandr Karpov that the budget cannot be built "on a virtual scheme from the very beginning, conceptually" and that there is no guarantee that "the revenues will actually take place" (UT-1, UTN-Panorama, October 13, 2000). Many MPs, from the left wing of the political spectrum as well as from the center and the right think that probably only one-third of the planned amount will also be reached; many MPs also doubt that the revenues, even if received, will be spent on enterprise development and financing of poverty reduction programs.

Yet, some politicians are optimistic about the privatization prospects. For instance, Oleksiy Kostusev, MP, believes that the government's estimates for the UAH 9.2 billion privatization revenue in 2001 is quite realistic (Den, October 18, 2000). According to chairman of the parliament's Budget Committee, member of Yulia Tymoshenko's Batkivshchyna party Oleksandr Turchynov, the only thing that may hinder the adoption of the 2001 budget in the first reading is "some political positions of certain factions, aimed not only against concrete proposals but against the government". Hence, the delay in the budget process may have a visible impact on the political appearance of the parliamentary majority and single out its "pro-government" part, notwithstanding the numerous statements of the parliament's leadership that the unity of the majority cannot be challenged by anything.

Another point of controversy is the fact that the inclusion of the privatization revenues to the budget runs counter the IMF's recommendations. Unlike the Ukrainian government, the IMF does not see the privatization money as a prime source of budget revenue for in most countries of the world (some Ukrainian politicians prefer to add "civilized world") the privatization money is used for development and enterprise modernization and restructuring instead of mending all sorts of public consumption "holes". In Ukraine's case, the latter looks likely to be the case, notwithstanding the government's "ten steps" announced by Prime Minister Victor Yushchenko as designed to ensure the fulfillment of the 2001 budget and transforming it into "the budget of development", for which as much as over UAH 3 billion would be channeled to the economic sector and the privatization money would not be "eaten up" (Ukraina Moloda, October 6, 2000).

Rather symptomatically, head of the State Property Fund of Ukraine Oleksandr Bondar admitted that the UAH 9 billion revenue, planned to be received from privatization, was a surprise for him and he was not sure that he would be able "to report successfully about fulfilling that plan" (Studio 1+1, TSN, October 17, 2000).

The law-makers' doubts about reality of the "virtual" draft budget were materialized in their decision to postpone the voting on the document in the first reading from October 19 to November 2. The parliament motivated the decision by the arrival of too many (about 6 thousand) comments and proposed amendments to the draft. The decision was preceded by the joint conference of the parliamentary majority factions with President Leonid Kuchma and Prime Minister Victor Yushchenko on October 18, 2000. Commenting on the meeting and its result, President Kuchma noted that he "did not give the task to convince members of the parliament to adopt the budget today". He described the meeting as a "frank talk" and stressed that the inflation rate included in the draft budget and the "mis-coordination" of the issue of relations between the national and local budgets "did not suit" him (Den, October 20, 2000).

However, postponing the voting date does not guarantee that the key financial document will be approved on time. The problem is not limited to the opposition of the left-wing part of the Ukrainian parliament. According to member of the Communist faction Georgy Kriuchkov, communists do not support the draft budget "on principle", for it has been formed "obviously not on a real basis". The claim is followed with traditional complains like "robbing the people even further" and "ongoing colonization of Ukraine" (Inter, Podrobnosti, October 17, 2000). After all, it is not unusual that left-wingers oppose privatization; the point is that the ranks of "left-wingers" tend to grow when voting on critical issues is at stake.

Problems of planning based on "recorded" achievements

While the current draft budget is zero-deficit, as demanded by the Budget Resolution adopted by the Ukrainian parliament in June 2000, a number of MPs are rather skeptical of accuracy of the "zero-deficit" claim because they think the privatization revenue task is too ambitious. For instance, leader of Vidrodzhennya Rehioniv Oleksandr Volkov argues that "we believe the budget contains built-in budget deficit, namely those 9 billion hryvnias" (Inter, Podrobnosti, October 17, 2000). According to the President's top economic adviser and chairman of the Supervisory Board of the National Bank of Ukraine Anatoly Halchynsky, the expectation to receive UAH 9 billion from privatization in 2001 are not convincing and even "artificial": "This figure is specified in the three-year privatization program that was approved by the Verkhovna Rada. Then everybody applauded. Now the government is taking measures to receive the UAH 2.5 billion planned for the current year (Vechirniy Kyiv, October 17, 2000). According to the Law "On the State Program of Privatization for 2001-2002, signed by the president on June 15, 2000, the amount of the budget revenues from privatization is expected to be equivalent to US\$ 1.5 billion and US\$ 1 billion, respectively. According to the 2000 budget, the revenue from privatization is to total US\$ 500 million in 2000 (Interfax-Ukraine, June 15, 2000).

Rather symptomatic data were quoted during the presentation of the formal report of the State Property Fund on October 17, 2000. According to the Ministry of Finance, since the beginning of this year the revenue from privatization has totaled UAH 1,283 million, while the initial plan from the ten months was to receive UAH 2,266 million (Den, October 18, 2000). In 1999, the revenue from privatization (less the money transferred by regional branches of the State Property Fund) totaled UAH 694 million against the UAH 800 million that had been initially planned. In 1998 the actual revenue from privatization was UAH 360 million, far less than the planned amount of UAH 1,040 million.

Hence, the repeated failure to meet the expected privatization objectives gives little reason to hope that the revenue part of the next year's budget will be fulfilled. This consideration - apart from publicly voiced doubts that appear to be based on something more substantial than just mere unwillingness to privatize attractive objects - has been offered as an explanation for the MPs' demands to reduce the target revenue from privatization by UAH 2.2 billion. On October 18, 2000, Victor Yushchenko stated that "when the draft state budget is upgraded <...> its revenue part will not be reviewed." On the same day Minister of Finance Igor Mitiukov announced that "... the Minfin [i.e., the Ministry of Finance] has been authorized to consider how realistic the revenue of UAH 9.2 billion from privatization is <...> Only the funds the receipt of which is guaranteed should be kept in the revenue part of the budget, while the rest should be kept out of it and channeled <...> for servicing the state debt." One week later, on October 25, Valery Asadchev, MP, announced that "... the government and the parliament reached preliminary agreement on reducing the figure of privatization revenue in the draft state budget <...> by UAH 2.2 billion." However, no official announcement of such an agreement has been made.

Privatize or Give Away?

These days the issue of privatization has been accompanied with at least two rather massive PR campaigns. On the one hand, the government takes every effort to demonstrate that any doubts about its ability to receive the necessary amount to the budget as revenue from privatization are groundless. The process of looking for potential investors interested in taking part in privatization of seven of Ukraine's regional electricity distribution companies, oblenergo, is gaining increasing publicity. Privatization of the oblenergo is one of the IMF's conditions for de-freezing its loan-making facility for Ukraine, and of

the EBRD for providing loans for completing reactors of the Rivne and the Khmelnytsky nuclear power plants, which itself serves as a strong motivation for the pursuit of the "energy privatization". Currently the second wave of privatization of oblenegos is gaining momentum, after the State Property Fund suspended sales of shares of nine oblenegos at the stock exchange and within the independent stock market in December 1999. The process was resumed shortly, in early 2000, but under new conditions including, primarily, transparency and search for "strategic" potential buyers.

On October 12, 2000, the government's session approved conditions of privatization of seven Ukrainian oblenegos, setting the minimum price for the seven lots of shares at US\$ 132 million, but actually planning to receive much more: about US\$ 250 million. All of the oblenegos are supposed to be privatized together with their debts to the budget that currently total almost UAH 1 billion. New owners of the oblenego are supposed to pay the debts within five years and can expect special beneficial arrangements for the initial two years.

On October 20 Prime Minister Victor Yushchenko personally advertised the oblenegos to potential Western investors. His negotiations with the leadership of the Silk Road (USA) were attended by representatives of the Credit Swiss First Boston, the official advisor to the Ukrainian State Property Fund (SPF) in the matter of privatization of the seven oblenegos. According to SPF head Oleksandr Bondar, the Prime Minister's "road show" could be described as a success, as two major Western companies, Electricite de France and the American AES Silk Road confirmed their interest to bid.

Conditions of privatization of the first group of oblenegos - the Kyivoblenego, the Zhytomyrobolenego and the Rivneoblenego - were published on October 25. The sale is expected to bring over US\$ 100 million. The start prices have been established at US\$ 32 million for the Kyivoblenego, US\$ 18 million for the Rivneoblenego and US\$ 16.5 million for the Zhytomyrobolenego. According to Oleksandr Bazarov of the Credit Suisse First Boston, the privatization effort can be regarded a success on several conditions: if at least four companies are sold, if the privatization is fair and transparent, if the one to offer the highest price actually becomes the winner (DINAU, October 25, 2000). Currently the list of potential investors lists almost 40 companies prepared to bid.

This step, made by the cabinet of Ministers, may be regarded as a "trump card" used to impress the parliamentary majority before the draft budget debates, as the successful adoption of the budget may have a significant impact on this Cabinet's future. Yet, the successful privatization is necessary for something far more significant than security of some jobs in the government or the future of the oblenegos: the failure to meet the privatization revenue target specified in the draft budget may plant a time mine under the country's general social-economic status, no matter what exactly will be underfunded as a result, the traditionally cash-strapped social security programs or the state debt.

The second, equally dynamic PR campaign is remarkably symptomatic in this context, for it is aimed at convincing everybody that it is impossible to receive UAH 9 billion from privatization next year. One can add: impossible, if the proposal of not-so-attractive property is accompanied with not-so-attractive conditions. The efforts taken to convince the general public and potential buyers that Ukraine does not have any top-rate property to privatize and that whatever is offered for privatization is not worth much look irrational not only from the perspective of the need to receive as much money to the budget as possible, but also from the point of common sense, and raise suspicion that the seller - in this case, bureaucrats who act on behalf of the Ukrainian state - simply wish to reduce the price. The question "why" sounds rhetorical in this context: one may just remember the rapid reduction in the price of the Ukrainian telecommunications monopoly, Ukrtelecom.

Obviously, as regional electricity distribution monopolies, oblenegos will always be attractive pieces of property. However, there is a number of objects that are far more attractive and that could well be sold for more than the notorious UAH 9 billion. Yet, they may find themselves under the new ownership in a while: quietly, without too much public attention, through non-monetary methods and netting for past debts. These objects include strategically important pipeline systems, pipe-making plants, oil refineries, aluminum and nickel plants, granite quarries. Political and economic aspects of their property change is a matter of a separate research - particularly given the interest of one of Ukraine's "strategic partners" that simultaneously happens to be its most demanding creditor which may, with the little help of its local lobbyists, leave Ukraine no choice as to whether to privatize to or give away.

Any alternatives? Questions without answers

Obviously, it will be impossible to fulfil the budget without the due revenue from privatization. Notwithstanding all efforts taken by the Ukrainian taxation authorities to increase the level of tax collection (even though that many real business taxpayers simply cease to exist afterwards, and, naturally, pay no more taxes), the revenue from taxation can only be increased after the large privatization attracts massive investment and after the general business activity grows. For instance,

business activity can be stimulated - and, therefore, budget revenue increased - by opening road concessions and developing the road infrastructure and the system of transit transportation routes. However, even under the best-case scenario it is impossible to expect the return at once.

Apart from privatization and taxes, the budget revenue could include dividends that the state - still the biggest property owner in Ukraine - could earn on its shares. So far the real figures in this field remain a closely guarded secret. Remarkably, the dramatically low level of dividends has caused no reaction of the government. Notwithstanding the widespread belief that state-owned enterprises give no dividends because they do not work effectively, the real reason may be different: their top managers have no motivation to show dividends because they bear no responsibility for ineffective management and the resulting losses.

Another unanswered question is why, given the persistent shortage of budget revenues, the state privatizes so little and so slowly, and shows remarkably little interest in making its own property work effectively and bring dividends. The exulted debates about the "unrealistically high" amount of UAH 9 billion (about US\$ 1.5 billion) demonstrate the real problem of Ukrainian privatization, as the figure appears to be high only if compared to the modest achievement of the previous years. Yet, the debates suggest another option: in fact there is no intention to accelerate the pursuit of the large privatization, lose control of, and sell attractive pieces of property, search for the notorious "effective owner" and "industrial investor", and demand real dividends on the state-owned shares. The dilemma may confirm the claim that "the state" is not effective "in general", but effective are the individuals in the governance system who pursue their own interests.

Another issue that seems to need a logical answer is why little action is taken and few changes are made notwithstanding the repeated failure to meet the privatization tasks and criticism of the privatization process. The answer, almost classic, is "because someone needs it that way". The key problem of privatization Ukrainian style is the substitution of the critical element - the transfer of property rights and the arrival of an owner that would manage his/her property effectively and develop it - with the nomination of individuals that only pretend they have the property rights.

Unless the State Property Fund and other state agencies are brought to the condition that would be adequate to the large privatization task, start active preparation of the objects to be privatized, search for potential investors and introduce transparent competition procedures, until the property rights cease being a potential matter of revision, unless the category of face-figure "owners" backed by "higher" interest groups for re-distribution of public resources is minimized, it will be difficult to expect serious income from privatization, and even more difficult to expect successful market transformation.